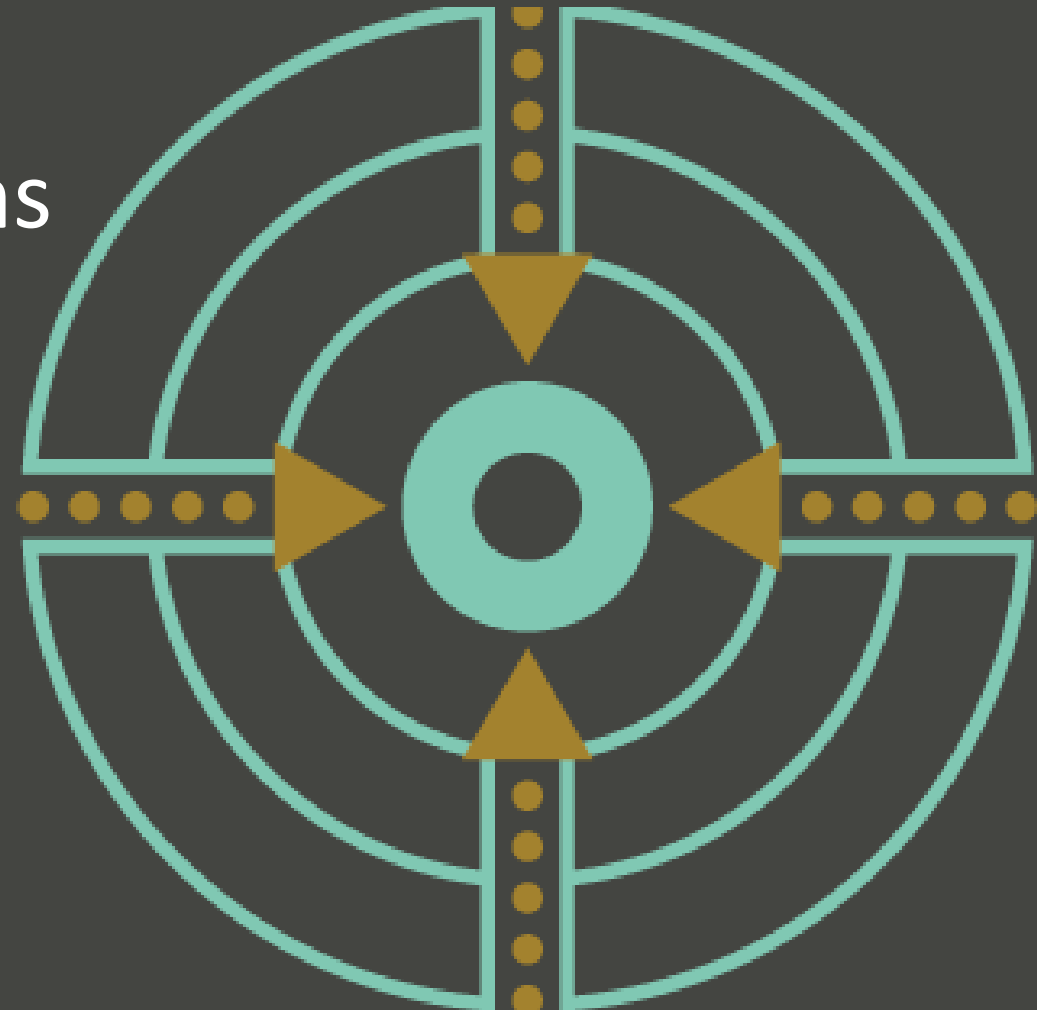


BEPS Pillar 2 Charging Mechanisms

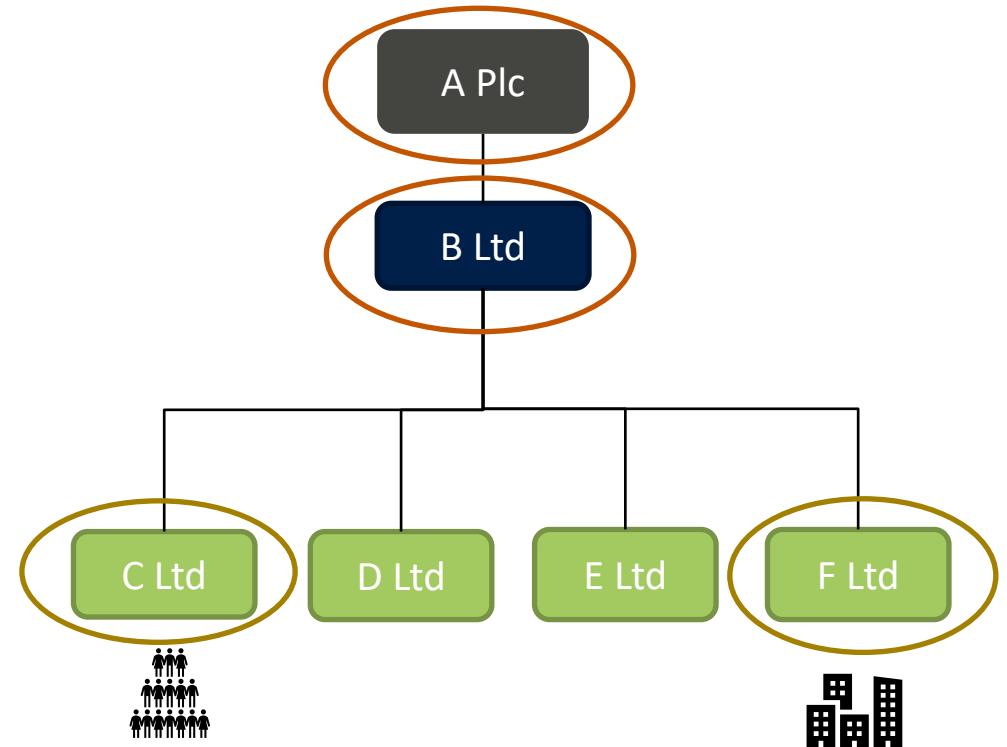
LAURA HODGSON

16 JUNE 2022



Overview

- **Primary charging mechanism: Income Inclusion Rule (IIR)**
 - Parent entities
 - By reference to Ownership Interest
- **Secondary charging mechanism: Undertaxed Payment Rule (UTPR)**
 - Constituent Entities in jurisdiction with employees and / or tangible assets
 - No required link to low-taxed constituent entity (LTCE)



Key definitions

- **Group**
 - Entities included in consolidated financial statements of Ultimate Parent Entity
- **Controlling Interest**
 - Hold Ownership Interest in another Entity
 - Required to consolidate income, assets etc of that Entity on line-by-line basis
- **Ownership Interest**
 - Equity interest carrying rights to profits, capital or reserves of an Entity

Group

A collection of Entities that are related through ownership or control such that the assets, liabilities, income, expenses and cash flows of those Entities:

- (a) are included in the Consolidated Financial Statements of the Ultimate Parent Entity; or
- (b) are excluded from the Consolidated Financial Statements of the Ultimate Parent Entity solely on size or materiality grounds, or on the grounds that the Entity is held for sale

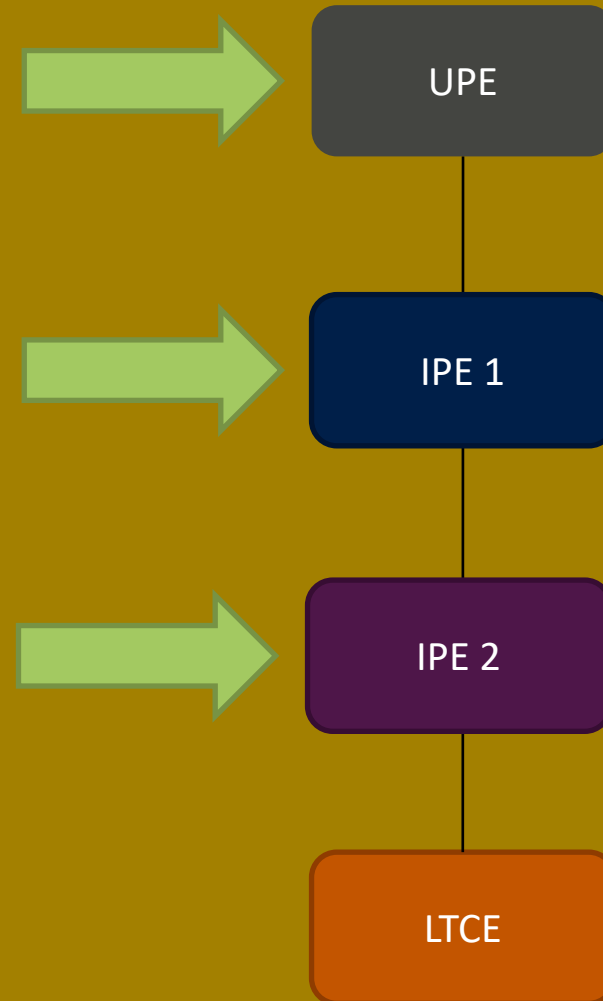
Key definitions

- **Ultimate Parent Entity (UPE)**
 - Owns a direct / indirect Controlling Interest in another Entity
 - Another Entity doesn't hold a Controlling Interest in it
- **Intermediate Parent Entity (IPE)**
 - Constituent Entity owns Ownership Interest in another Constituent Entity
 - Not: UPE / POPE / PE / Investment Entity
- **Constituent Entity (CE)**
 - Entity that is a member of the Group
 - Not an Excluded Entity
- **Low Taxed Constituent Entity (LTCE)**
 - Constituent Entity located in low tax jurisdiction
 - Effective tax rate lower than minimum rate



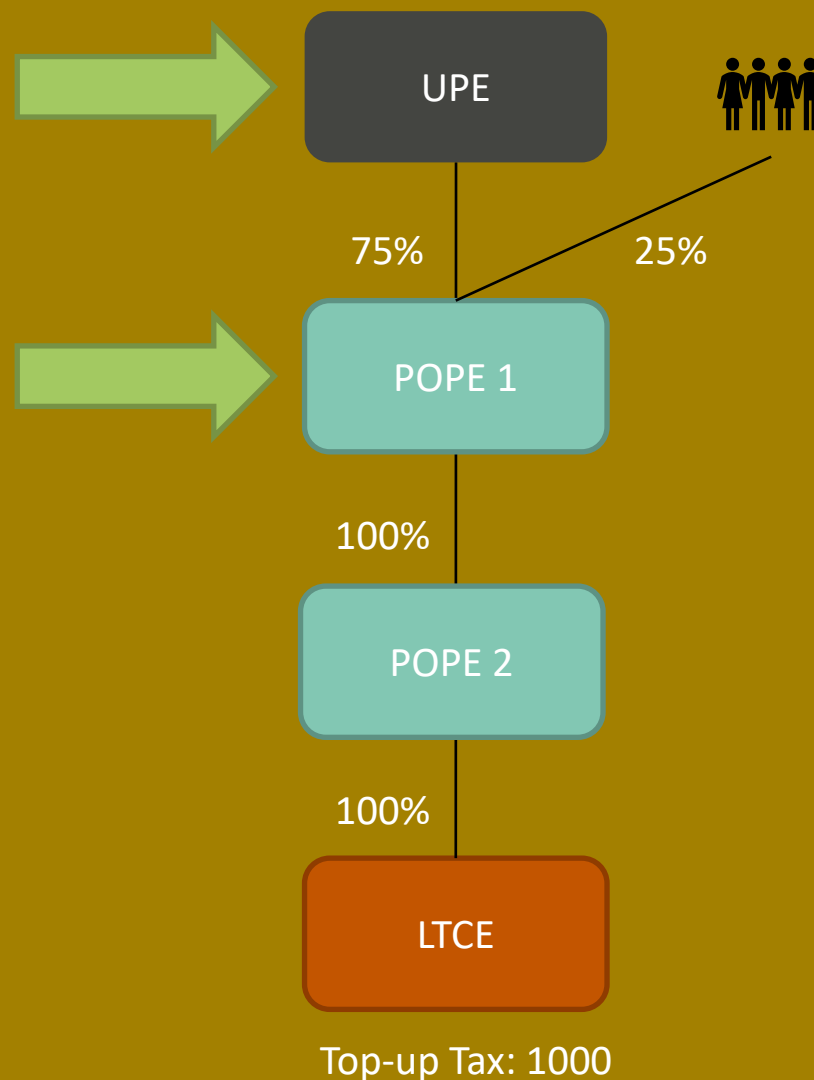
IIR: Basic Rule

- **UPE Charge**
 - Must hold Ownership Interest in LTCE at some point in Fiscal Year and be in IIR jurisdiction
- **Parallel IPE Charge**
 - Must hold Ownership Interest in LTCE at some point in Fiscal Year and be in IIR jurisdiction
 - Disapplied if UPE / higher IPE required to apply IIR
 - % interest held by IPE is irrelevant to **whether** there is a charge (but taken into account when assessing quantum of charge)



IIR: Special POPE Rules

- Partially Owned Parent Entity (POPE): Constituent Entity (not a UPE) that holds an Ownership Interest in another Constituent Entity and more than 20% of it is held by 3rd parties
- IIR charge on POPE that holds an Ownership Interest in a LTCE at any time in a fiscal year
- Rationale: enables collection of more tax
- Double taxation issue dealt with under IIR Offset Mechanism



IIR: Domestic Top-up Tax

- Parent Entity only required to apply IIR to LTCEs in other jurisdictions – Article 2.1.6
- Commentary - Implementing Jurisdiction can depart from this and collect top-up taxes attributable to:
 - Domestic LTCEs
 - Parent Entity



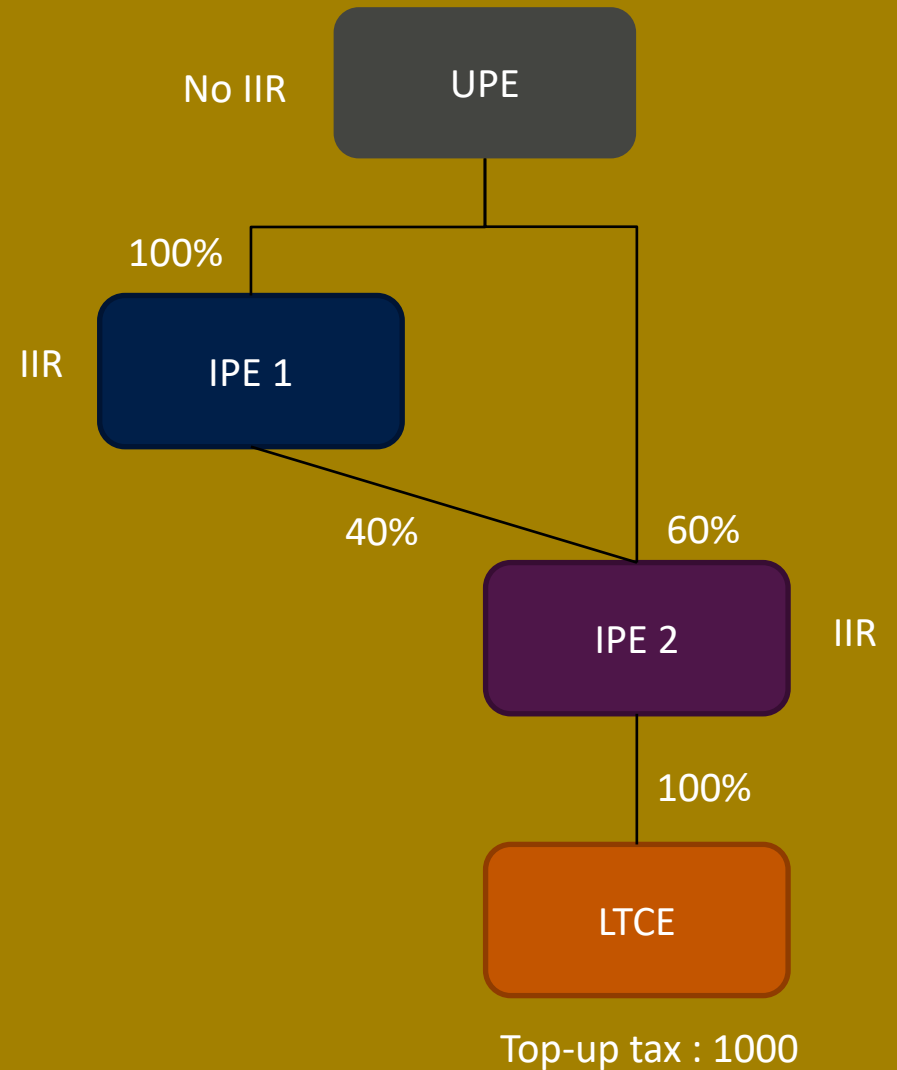
IIR: Allocable Share

- Top-up tax payable under IIR restricted by reference to Parent Entity's interest in LTCE
- Allocable Share = Top-up Tax of LTCE x Parent Entity's Inclusion Ratio
- Inclusion Ratio
 - Deduct share of LTCE's GloBE Income attributable to any minority interests in LTCE
 - Use hypothetical consolidated accounts to assess amount attributable to minority owners



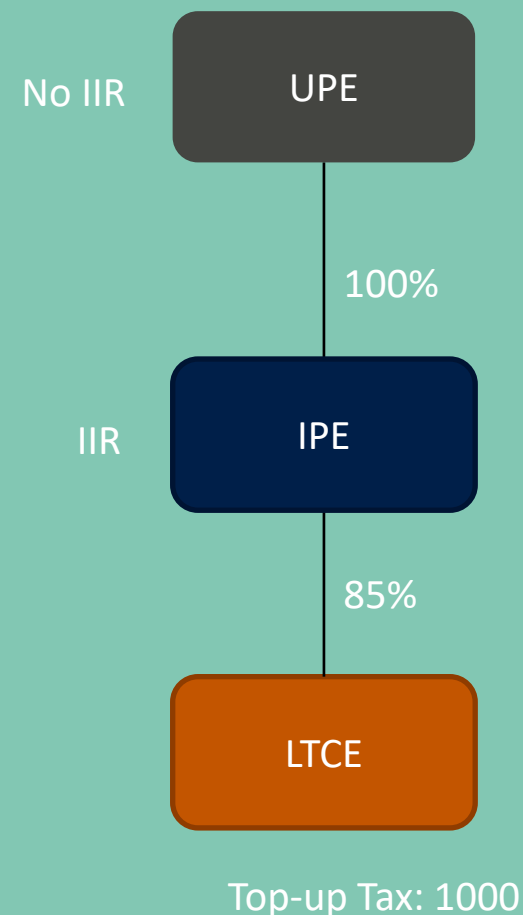
IIR: Offset Mechanism

- Mechanism to prevent double taxation
- Where Parent Entity holds Ownership Interest through IPE / POPE that is required to apply IIR, reduce Parent Entity's top-up tax liability by IPE / POPE's Allocable Share
- Applies on allocation, not payment



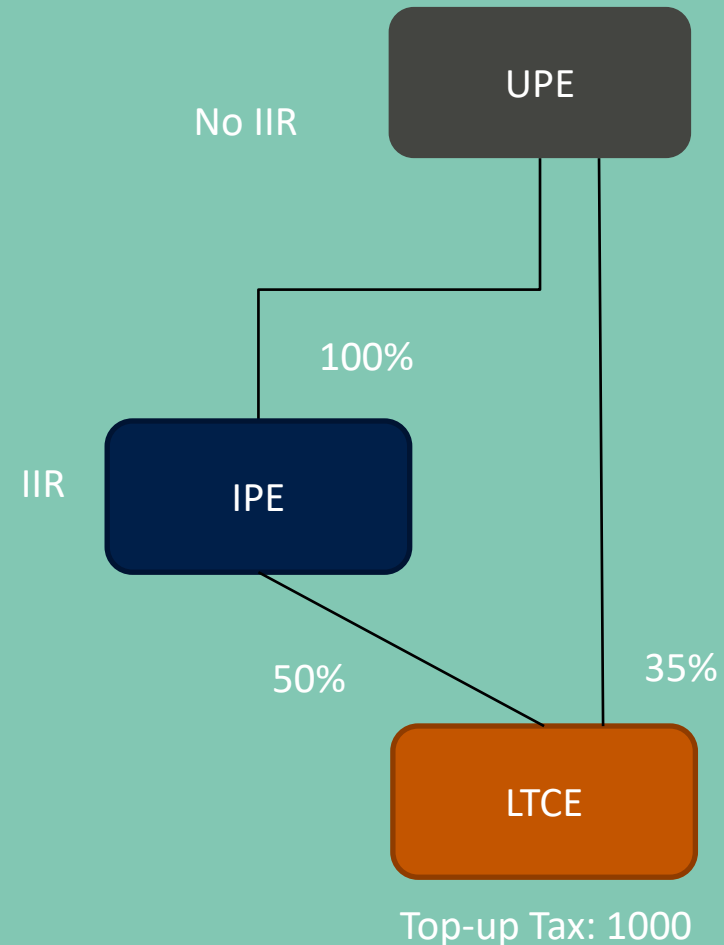
UTPR: How much?

- UTPR Top-up Tax Amount = Total Top-up Tax for LTCEs
- Two offset mechanisms:
 1. All of UPE's interests in LTCE are held through IIR jurisdictions: UTPR Top-up Tax Amount reduced to zero
 2. UPE's interests in LTCE are not all held through IIR jurisdictions: UTPR Top-up Tax Amount reduced by IIR charge
- Assess offset mechanisms on entity by entity basis



UTPR: How much?

- UPE's interests in LTCE are not all held through IIR jurisdictions: UTPR Top-up Tax Amount reduced by IIR charge
- Leaves within charge low-taxed income beneficially owned by persons outside MNE Group
- Punitive where LTCE is a Minority Owned Constituent Entity



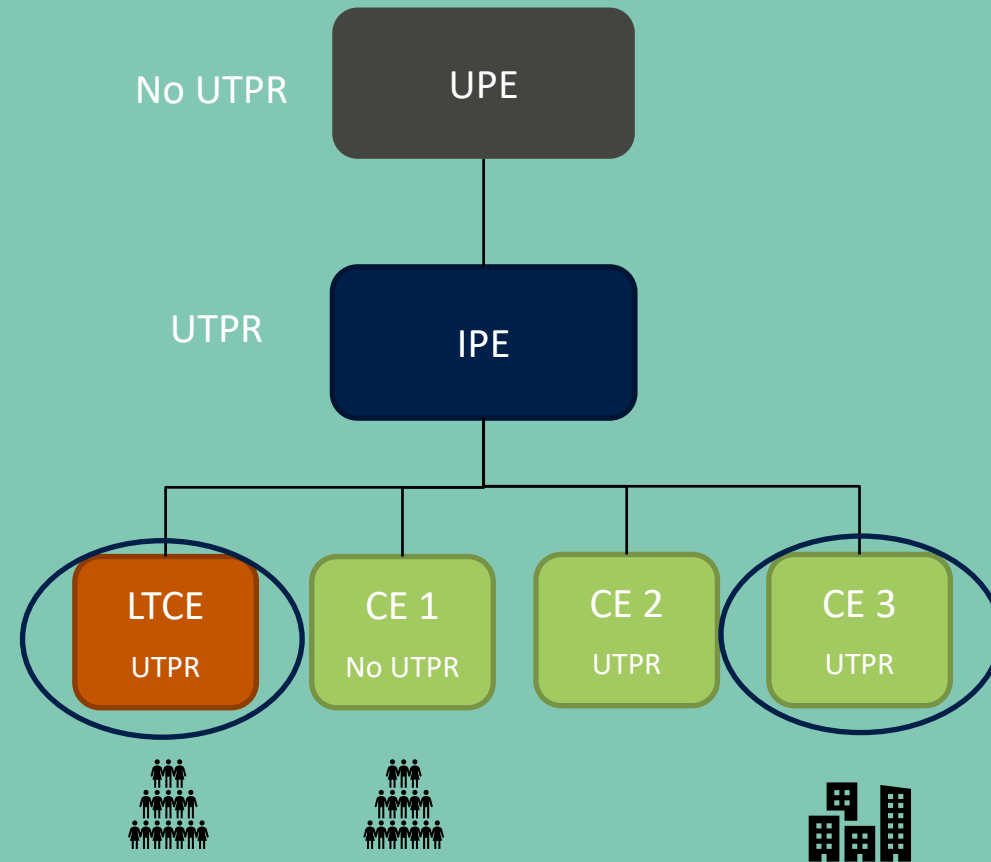
UTPR: Operative mechanism

- Choice given to implementing jurisdictions
- Option 1: denial of deduction
- Option 2: alternative adjustment that results in cash tax expense
- Carry forward mechanism
- Maximum amount must be collected as early as possible



UTPR: Allocation between jurisdictions

- UTPR Top-up Tax Amount allocated to jurisdictions that have implemented UTPR and have employees and / or tangible assets
- UTPR Percentage =
 - 50% of Employees in Jurisdiction / Employees in UTPR Jurisdictions; and
 - 50% of Tangible Assets in Jurisdiction / Total Tangible Assets in UTPR Jurisdictions
- Don't allocate to jurisdictions that haven't yet recovered allocated UTPR Top-up Tax for a previous year



UTPR: Allocation between entities

- Implementing jurisdictions given choice how to allocate between Constituent Entities in their jurisdiction
- Must collect maximum amount as early as possible
- Profitable v loss making entities?
- Wholly owned v minority entities?

